

Rev. Rul. 64-231, 1964-2 C.B. 139, distinguished Rev. Rul. 73-549

An entrance fee paid, in addition to a required lump sum life-care payment, as a prerequisite to obtaining direct personal services and residence in home for the aged, must be included along with the required lump sum life-care payment to the home in determining whether the home renders services to all or a reasonable proportion of its residents at substantially less than its cost, to the extent of the organization's financial ability, for purposes of qualifying as an exempt charitable organization described in section 501(c)(3) of the Internal Revenue Code of 1954.

In making such a determination, the total payment may be amortized over the remaining life expectancy of the residents as of the date of entry into the home. The life expectancy tables applicable to annuities under section 1.72-9 of the Income Tax Regulations may be used for this purpose.

Advice has been requested regarding the treatment of certain payments made to a home for the aged, in order to determine its eligibility for exemption from Federal income tax as a charitable organization described in section 501(c)(3) of the Internal Revenue Code of 1954.

Revenue Ruling 61-72, C.B. 1961-1, 188, holds that, if otherwise qualified, a home for the aged is exempt from Federal income tax under section 501(a) of the Code as a charitable organization described in section 501(c)(3) thereof, if (1) it is dedicated to providing, and in fact furnishes, care and housing to aged individuals who would otherwise be unable to provide for themselves without hardship, (2) such services are rendered to all or a reasonable proportion of its residents at substantially below the actual cost thereof, to the extent of the organization's financial ability, and (3) the services are of the type which minister to the needs and the relief of hardships or distress of aged individuals.

The instant organization is, in effect, organized for the same purposes and operated in the same manner as the organization in Revenue Ruling 61-72, and similarly meets parts (1) and (3) of the criteria for exemption set forth in that ruling. A question arises, however, concerning payments required by the organization as a prerequisite to obtaining residency and direct personal services at the home, and the manner in which such payments are to be treated in determining whether the organization meets criterion (2) above, i.e., whether it renders services to all or a reasonable proportion of its residents at substantially below cost, to the extent of its financial ability.

Specifically, the home requires payment, at the time of acceptance of a new resident, of an entrance or membership fee by or on behalf of the new resident. In addition, lump sum life-care payments are required to be made. These latter payments are

designed to cover care for life, determined on an actuarial basis.

The question presented is whether the entrance fee should be eliminated in determining whether the organization renders services to all or a reasonable proportion of the residents at substantially below the cost thereof, to the extent of its financial ability.

The organization contends that it treats entrance fees as capital contributions to be used in the reduction of capital costs such as depreciation and, accordingly those fees should be eliminated from consideration in determining whether the life-care payments are substantially less than cost.

However, it is stated in the written agreement between the organization and the resident that the entrance fee and life-care fee are payments by the resident to assist in the financing of the home. It is further stated therein that where a resident is dismissed by the home a refund on the entrance fee and the life-care fee (if paid in a single payment) is predicated on an amount equal to the difference between the amount paid in and the amount used for the care of the aged person during the time of residency, based upon the per capita cost to the home. Provision is also made for a refund of a portion of the entrance fee and life-care fee, based on the period of occupancy, in case the resident desires to withdraw voluntarily from the home. In the event of death of a resident, all entrance fees and all funds deposited for the life-care contract of the resident remain the property of the home.

The entrance fee varies in accordance with the type of unit occupied by the resident. Residents are entitled to services as provided in the agreement but they acquire no title either legal or equitable to the real property or improvements of the home or to personal property or furnishings provided by the home. Thus, under the agreement the payment of the entrance fee entitles a resident to occupy particular accommodations at the home and to receive services there so long as he retains his 'membership' and pays the additional life-care fee.

Under these circumstances the payment of the entrance fee is merely a prerequisite to obtaining direct personal services at the home. Accordingly, such fee cannot be regarded as a capital contribution; rather, it is an amount paid to entitle a resident to enjoy the facilities of the home representing, in effect, a part of the payment for services rendered to him there. The entrance fees, therefore, being just as clearly payments for services rendered to the residents as are the life-care payments, must be taken into account in determining whether services are rendered to all or a reasonable proportion of the residents at substantially below the actual cost thereof, to the extent of the organization's financial ability, as required by the criteria referred to above.

For purposes of this determination the entrance fees and lump sum life-care payments may be amortized over the period representing the actuarially determined life expectancy of each of the residents at the time of entrance into the home.

In determining the life expectancy of a resident of a home for the aged for the purposes set forth above, the life expectancy tables applicable to annuities under section 1.72-9 of the Income Tax Regulations may be used.